

Analysis of the Government Competition with Private Vendors Questionnaire

For the Business, Labor, and Agriculture Interim Committee

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INTRODUCTION

The Business, Labor, and Agriculture Interim Committee (Committee) developed a survey tool to assist them in defining and recognizing any competitive factors and exist between public agencies and private vendors. The survey was sent out to private vendors with the assistance of the Montana Chamber of Commerce, several industry associations, and the National Federation of Independent Businesses. Several questionnaires were mailed as requests were taken.

State government agencies¹ and local government entities were also surveyed. The League of Cities and Towns placed a copy of the survey in a regular mailing and the Legislative Services Division mailed questionnaires to the County Commissioners of the 56 counties. A total of 163 surveys were returned from both groups. As with most surveys, some were more detailed than others.

The analysis of the returns will be in a combination of charts and a written narrative describing the content of the responses. In some cases, those surveys that were returned via e-mail were copied verbatim into the paper. A few of the industries offered more detailed information than others. Those sectors were chosen for this phase of the analysis based on what seems to be their willingness to assist the Committee in developing findings and conclusions to this issue. In certain cases, there were so few individual responses by sector that their responses were included in a larger analysis of questions rather than offer the response of one member of the industry. It should be noted however, that most, if not all of the responses from these groups were generally within the range attributable to the larger response groups.

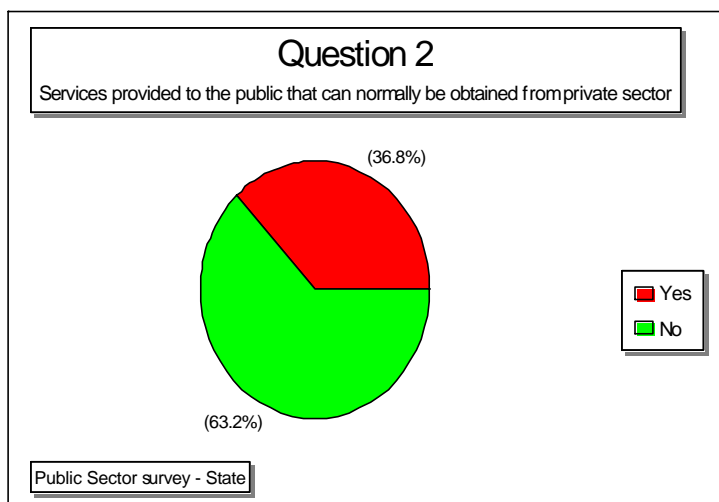
State Surveys

Though there were 21 questions designed to gather a broad perspective of state government's views on this topic, a handful of the questions can be viewed as more important than others for the purpose of establishing the Committee's future direction. For instance, questions 2, 4, 8, 12, 15, and 16 seek answers to pressing questions raised by the Committee. The companion questions to the scoping inquiries provides the Committee with a list of services that agencies have identified that are available from the private sector and the rationale, if any, an agency uses to make its decision to offer those services. Clearly, whether an

¹The following state agencies received Committee surveys: Administration, Agriculture, Auditor, Commerce, Corrections, DEQ, FWP, Justice, Labor, Livestock, Military Affairs, DNRC, OPI, DPHHS, Revenue, Secretary of State, Transportation, and the Governor's Office.

agency provides goods or services to the public or another unit of government that can normally be obtained from the private sector sets the stage for this analysis. The questions, and their accompanying charts, are found below.

Q2. Does your organization provide public goods or services that can normally be obtained through the private sector?

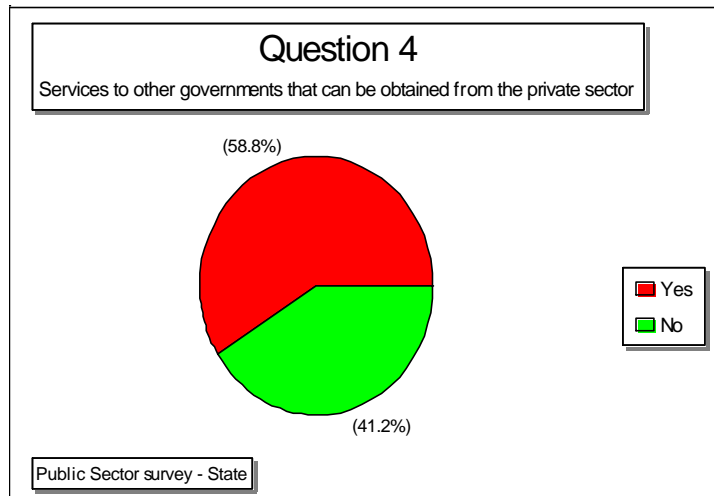


Those responding to the State public sector survey were asked the types of services that they engage in providing that could be normally obtained through the private sector. It was clear that using the phrase "normally obtained" created some concern among the respondents. The phrase was used to make a connection between the investigation conducted by the Committee and the language of House Bill No. 515 in its original form. It was also used to denote the fact that in many instances, services provided by the government may not be easily obtained from available private vendors, or the obtaining of certain services may not be cost-effective. This will be raised in greater detail during the discussion of local government responses.

The following represents the responses from the state agencies returning the survey:

- C Hail Insurance;
- C Workers' Compensation and Occupational Disease Insurance;
- C Collection, data capture, and forms development;
- C Computer programming;
- C Auditing and accounting;
- C System maintenance; and
- C Technical and financial assistance to businesses in conjunction with private providers.

Q4. Does your organization provide to other governmental entities goods or services that can normally be obtained through the private sector?

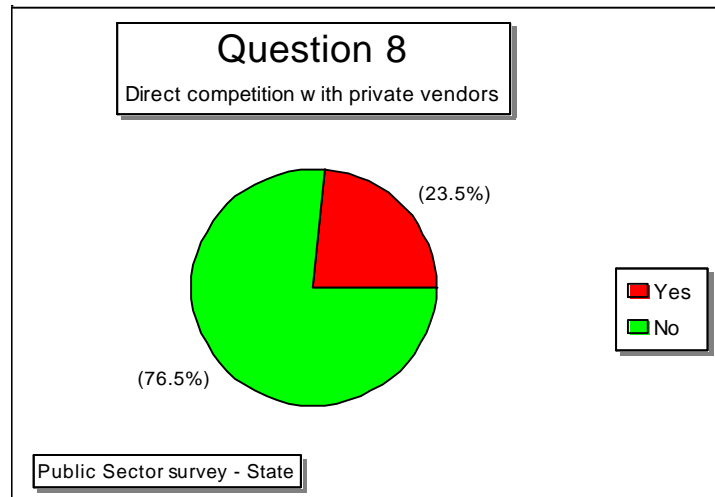


Again, agency respondents were requested to delineate the services that they provide to other governmental entities that may be normally obtained through the private sector. There is some overlap between those services provided to the public and those provided to public agencies. The following is a list of services identified in the state responses.

- Workers' Compensation and Occupational Disease Insurance,
- microfilming,
- records storage,
- state motor pool,
- aerial photography,
- occasional materials sales(not encouraged),
- printing, publishing, binding, office and computer supplies,
- painting carpentry, minor maintenance,
- computing services,
- telecommunications, and
- transaction processing, accounts receivable, registration and account maintenance.

Q8. Has your organization competed directly with a private sector vendor for the provision of goods or services?

This question represents the major issue behind the HB 515 study. The responses indicate that over 75% of the state agencies (13 Departments) returning the questionnaire do not actively compete with private vendors in service delivery arenas. The chart below represents the percentages.



The follow-up to Question 8 was designed to offer the agencies a chance to describe their rationale for engaging in competition with private vendors. The survey is limited in what information it can collect, as is the case in this instance. The information does allow decisionmakers to investigate these instances further and ask each agency, if determined to be appropriate, to better describe the conditions that resulted in their competing with the private sector. One question the Committee may wish to consider asking the agencies is whether they made an attempt to secure a private service provider and, for one or more of the reasons offered below, chose to continue to provide the service in-house. A second question to consider is whether the agency chose not to contract with a private vendor, but rather recognized a possible arena for service delivery and began to market its services. Both of the scenarios describe a competitive arena, but also represent a distinct decisionmaking methodology.

Those agencies that did respond offered the following points as their rationale for competing with the private sector.

- C cost;
- C quality of private vendor service;
- C dependability of vendors;
- C lack of a well-defined vendor pool; and
- C timing constraints.

Another example offered was that the state was selected as a service delivery option by a private vendor having control of non-state funding sources. What follows is a verbatim response from two state surveys.

To meet our statutory obligations we maintain an infrastructure to process high volumes of transactions. It is cost effective, and yet not used to capacity, so we bid a data capture job being considered to be placed with the private sector. The decision was made by the agency/customer on the basis of cost and convenience (Dept of Revenue).

...the State Fund is required by law to allow employers an option to insure their liability for workers' compensation and occupational disease coverage. The State Fund is also required to be self-supporting. To do so, the State Fund must compete for customers in order to have a mix of business that supports a solvent State Fund.

There are 27 state funds in the United States of which five are monopolies (employers must insure with the state fund or self-insure and coverage with a private carrier is not an option). Fourteen state funds serve as the insurer of last resort and must be competitive in price, product and service in order to write affordable coverage for any employer who requests coverage, regardless of size or risk. The eight remaining state funds, even though they have assigned risk pools, are designed to provide employers in that state a competitive option for their workers' compensation coverage.

Western states where competition with a state fund is allowed are Oregon, Idaho, Colorado, Arizona, New Mexico, Nevada and Utah, and in those states employers also stand to benefit from a competitive environment. In every state there is either a state fund to serve as the insurer of last resort or an assigned risk pool. State funds were created in eight states in recent years, and in six of the states the assigned risk pool was replaced with a state fund. Other private carriers have generally expressed opposition to an assigned risk pool in Montana. (State Fund)

- Q12. Describe the decisionmaking process that your organization employs to determine whether the delivery of services should be kept in-house or contracted out?

A number of considerations: Is it a core competency?; Do we have the capacity to satisfy the business requirement?; Cost/benefit review; and Scheduling/workflow/capacity (Dept. of Revenue).

As workers' compensation insurer, the necessity of maintaining a solvent State Fund and the needs of our customers dictate this business decision. Based on the type of service needed, the State Fund determines if the service can be effectively and efficiently delivered by in house resources or if the State Fund and its customers would be better served if the service was contracted out. Factors taken into consideration are the complexity of the project, the necessary expertise, the cost benefit, customer needs and the short and long-term need of the service. (State Fund)

Statutory sunset review by legislature has occurred.

Board of Hail Insurance annual meetings.

Subcommittee review by industry for policy sale by private insurance agents occurred in 1997. (Department of Agriculture)

The first step is to identify our needs. We create a plan that includes the resources necessary to complete the tasks. If it is determined that we do not have the needed resources in-house, we begin the process of looking at the private sector. We take considerable time at this point and complete an in-depth cost analysis. Utilizing the plan, we then examine the state term contracts and see if there are vendors that can provide the needed service. If so, we examine those first, having meetings with all that fit the criteria. If not, we put the plan – thus the RFP – out to bid. (Secretary of State)

Public Safety - some public safety activities should not be privatized.

Quality - where quality is as good or better the activity has been contracted. If quality is not maintained, by the private sector, the activity will be retained in-house.

Efficiency - when private sector efficiency is as good or better than in-house the private sector has been used. The scale of a project affects efficiency and may be done in-house.

Cost - private sector used when cost effective. In some cases cost may not be the total issue i.e. production of aggregates and/or hot mix. These activities require costly specialized equipment and highly trained mobile work forces and the department has totally contracted these services rather than perform them in-house.

Contractor Availability -- are contractors available (geographical or quantity) and can they perform the activity within time requirements. Montana is a large state with a limited season to perform many maintenance activities.

Work Load - the department is a lean organization and does not always have the required staff to accomplish an activity and activity is contracted with the private sector.

Enforcement - of truck laws, licensing power units for interstate travel and issuing oversize permits. (MDT)

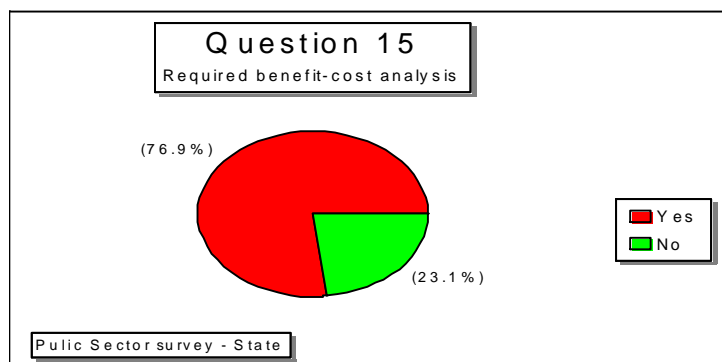
The decision is based on job complexity, delivery requirements and cost (Department of Administration -P&P).

Each potential project is analyzed individually. If it is small, and we have resources available, we may do it in-house. If it is more than very minor maintenance, we go to contracting (Department of Administration - General Services).

ISD management regular assess the mix of services that should be provided by the division, using a number of criteria to determine how services will be provided:

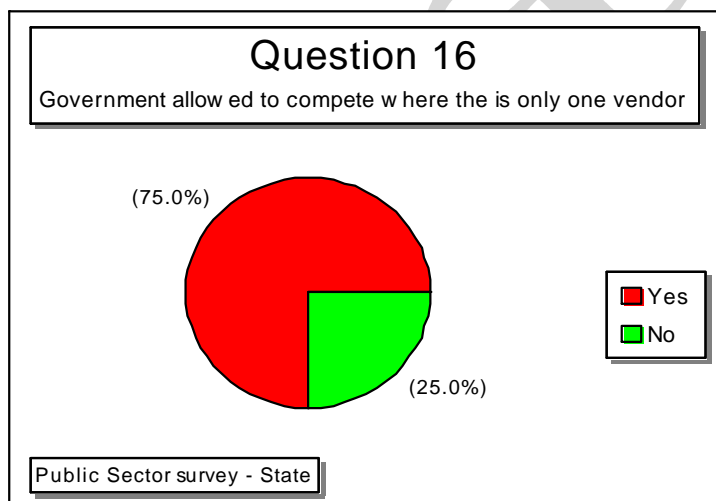
- a. *Expertise--ability to acquire and maintain sufficient expertise.*
- b. *Volume--sufficient need to establish a service*
- c. *Financial viability—ability to provide a service at a reasonable cost to private sector alternative*
- d. *Control--need to retain control, especially ready access to a service when needed, of a key function/support function within government*
- e. *Cost--ability to acquire the service at a reasonable cost from other sources*
- f. *Priority--importance of the service relative to other services within budgetary or other resource constraints*
- g. *Technology Life Cycle—"dead" or "dying" technologies are often considered for outsourcing to companies with a larger base of volume to maintain lowest possible rates for services*

Q15. If government has been asked by the public within its jurisdiction to provide a service or product, should government decisionmakers be required to conduct a benefit-cost analysis to determine who provides the services (e.g., public or private vendors)?



Responses to this question were generally followed by a descriptive qualifying statement. The question clearly asks whether the government service provider should be required to conduct a benefit-cost analysis to determine *who provides the service* (emphasis added). It is presumed that an agency would conduct some analysis to determine organizational structure, the costs associated with implementing the program, and any performance standards to determine the effectiveness of the program. However, without a specific directive to include delivery options in the analysis, the agency may not consider whether an available private vendor pool is capable of either partnering with the state agency or simply awarded a contract to be the sole service provider. Again, the question was designed to achieve a first impression. There is no indication from the responses or any other information that would suggest that agencies do not conduct this kind of analysis currently.

Q16. If there is only one private provider of a particular product or service, should government be allowed to compete with that vendor?



Like the previous question, several respondents offered a comment to clarify their position or suggest that the question was too broad for them to effectively respond. The question was asked to determine whether agencies used a "sole vendor" condition as justification to either compete with the private sector or continue to offer services in-house. The literature on privatization suggests that decisionmakers should be mindful of creating monopoly private service providers but does not suggest that to allow the creation of monopoly providers would regularly create performance or accountability concerns. This question was also designed to spur discussion of the potential benefits of competition, whether among private vendors or among public and private entities.

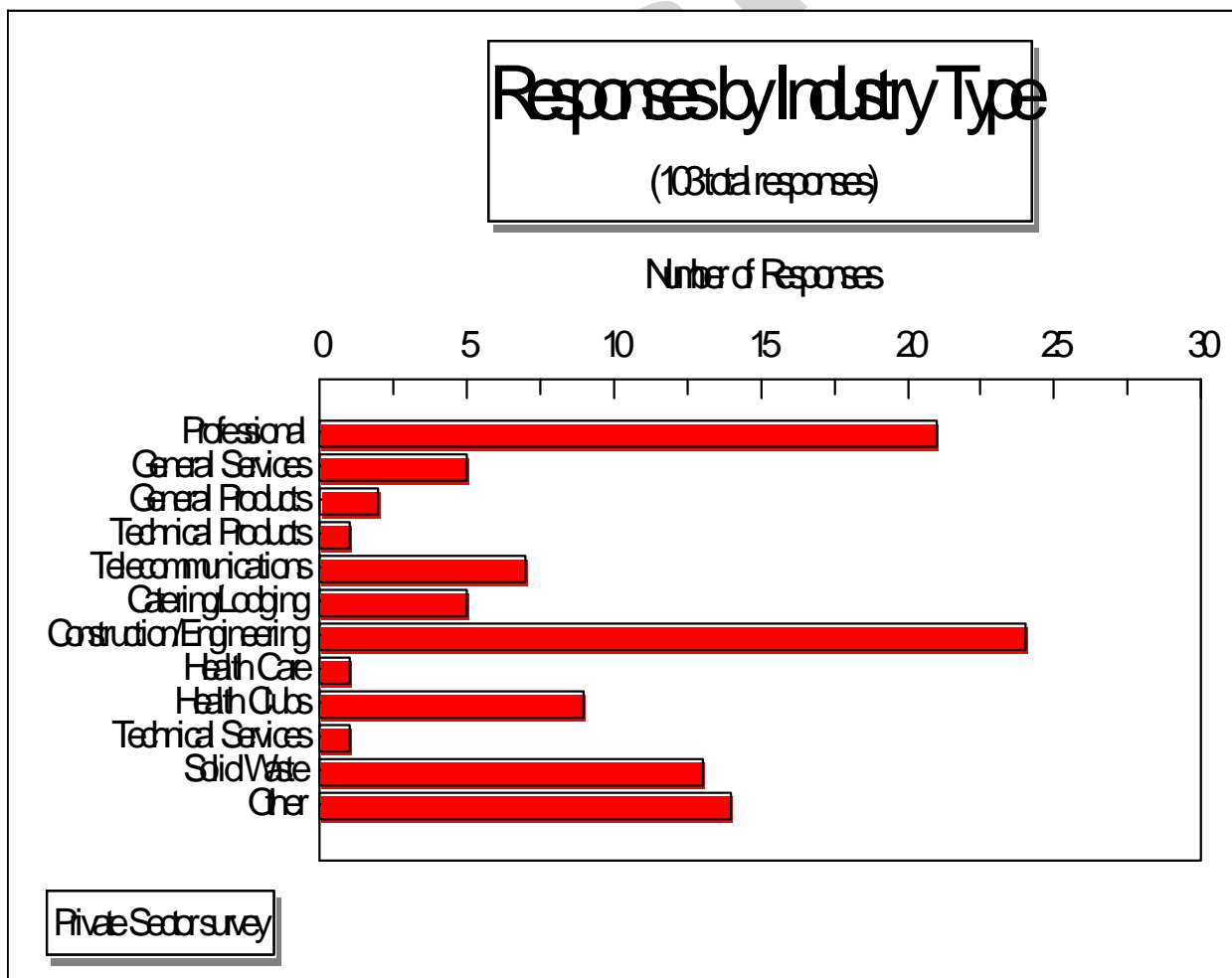
The questions pertaining to the implementation of benefit-cost analyses and the regular review of service delivery policies and procedures creates an opportunity for the Committee to begin the discussion of determining how the state agencies make decisions related to delivering a service. Clearly, requiring state agencies to conduct a benefit-cost analysis would require additional resources dedicated to the development of these analyses. However, this question also attempted to illicit responses about whether, if an agency has made a decision to contract a service, any analysis was conducted.

PRIVATE SECTOR RESPONSES

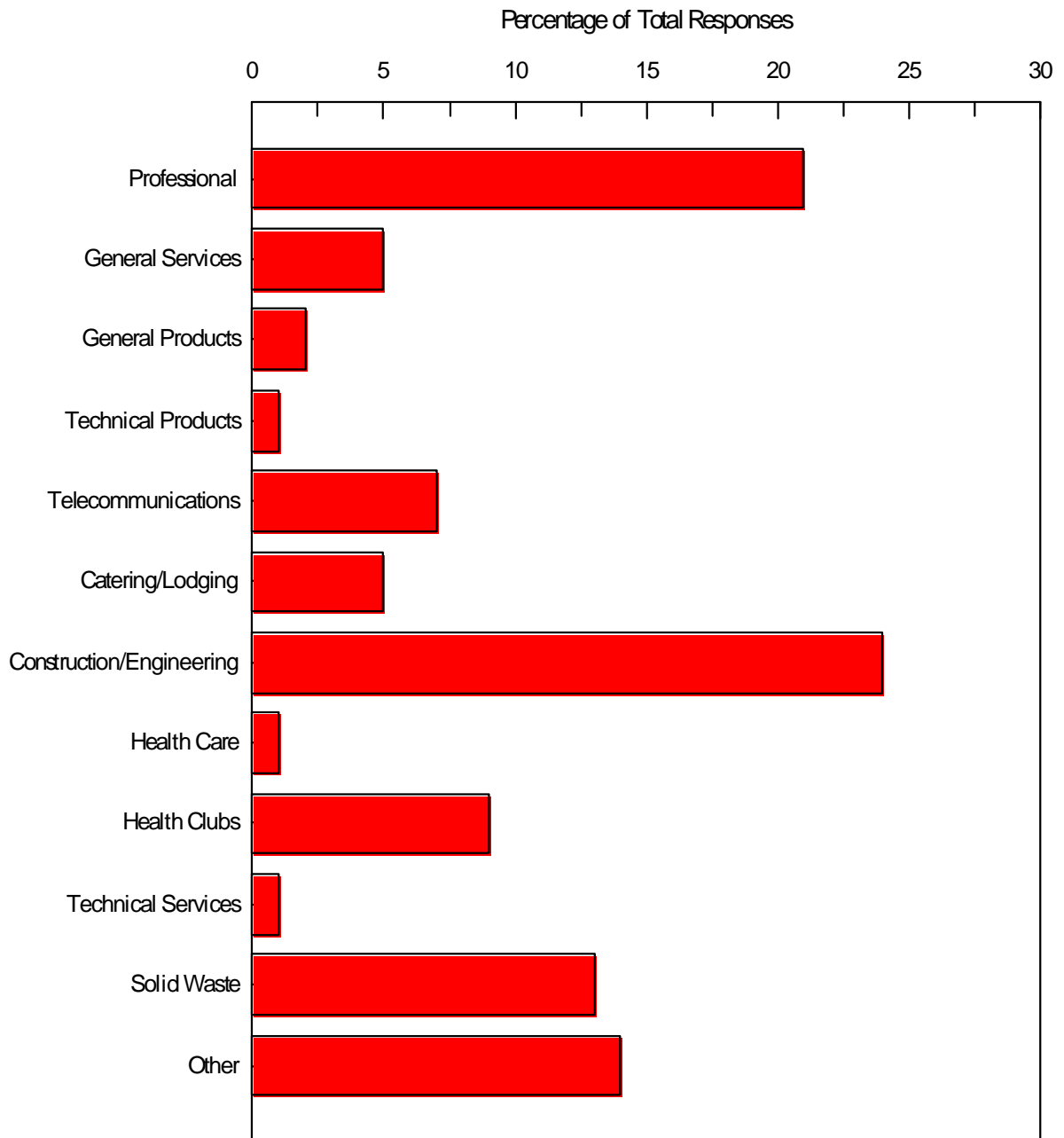
A wide variety of vendors responded to the survey. However, the percentage analysis of the private sector responses will be presented in the aggregate unless the number of respondents within an industry offers an

important concept of the Committee's work to date. It is difficult to determine whether the returns by industry can be viewed as a representative sample (just one of the many limitations of this questionnaire), or whether those industry members that did respond are willing to contribute to the Committee's deliberation. In either case, the survey was designed to offer the Committee with a broad sense of the competitive conditions in Montana, and isolate perhaps, problems that may be candidates for legislative recommendation. The construction/engineering industry returned 24 responses. Professional services, which includes responses from private insurance providers followed with 21 questionnaires. The remaining responses by industry are shown in the chart below.

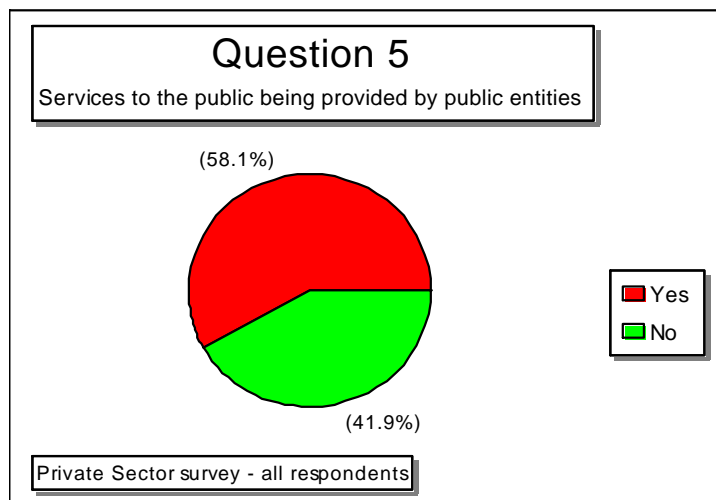
In terms of percentage of responses by industry, the Construction/Engineering industry led the returns with approximately 25 percent. Professional services followed with just over 20 percent. Solid waste and the Other category responded between 13 and 15 percent. The remaining industry's were less than 10 percent of the total. Once again, based on the fact that it would have been difficult to control the size of the sample, this survey tool was not designed to generate statistically significant data. It is beneficial, however, to view the percentage of responses of each industry type. Doing so may demonstrate that certain segments of the private sector may have a deeper concern with public/private competition than others. The remaining percentages are outlined in the chart below.



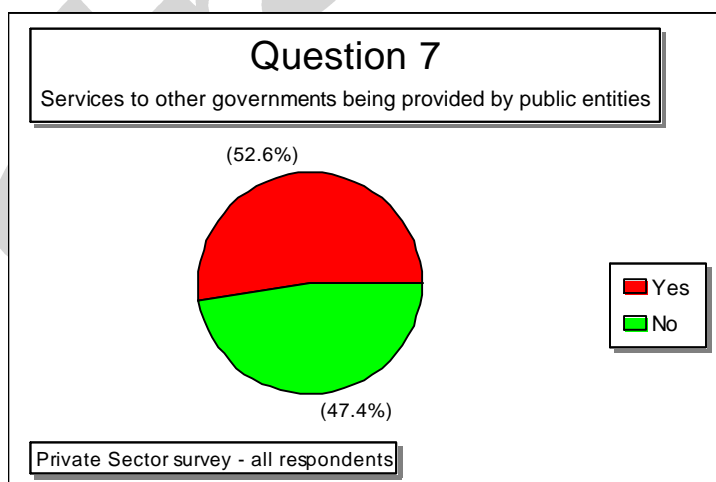
Private Sector Industry Survey



The following three charts represent the private sector returns responses to questions 5, 7, and 9 in the aggregate.



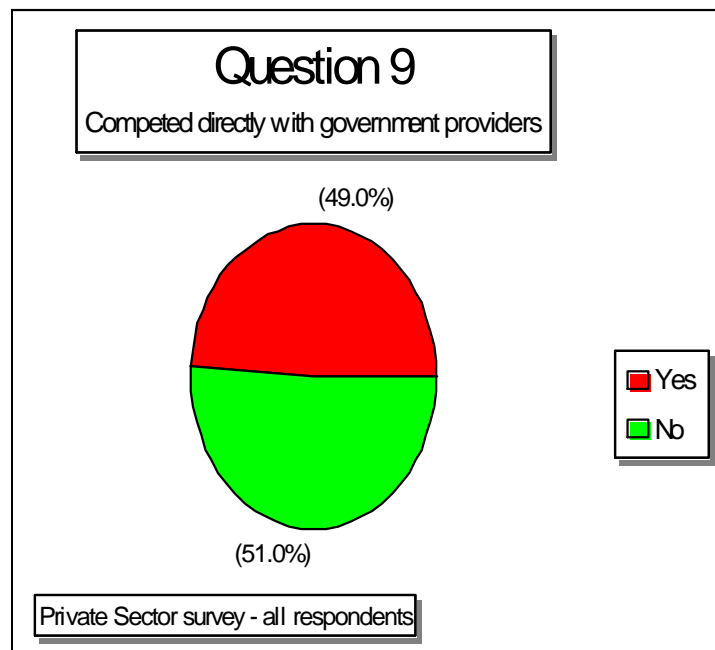
Q5. Does your organization provide directly to the public goods or services that are currently being provided by the government?



Q7. Does your organization provide to a governmental entity goods or services that are currently being provided by other governmental entities?

draft

- Q9. Has your organization competed directly with a governmental entity for the provision of goods or services?



The responses to question 9 seem to suggest two things. First, widespread competition between government entities and private sector vendors may not be occurring. However, the survey pool may not accurately reflect the true conditions in Montana. It will be clear in later analyses that in many instances, certain industry segments do state that they are facing government competition. The second suggestion may be that competition has been too broadly defined, or in some cases, too ill-defined to make reasonable decisions about potential remedies. In essence, competition seems to mean something different to each person responding to the survey. In some cases, respondents, both public and private, identify cases where two entities compete head-to-head for customers. In others, references to competition means that both parties provide the same service, regardless of whether any direct competition is occurring. Both viewpoints represent a valid concern. However, a single legislative remedy may not be able to meet the needs of the two interests. Further discussion of this issue will be critical for establishing the Committee's recommendations.

Telecommunications Providers: Highlights and Recommendations

It should be noted that while not all respondents believed that the state was competing with them, each made reference to the possibility that this Committee could make recommendations to ensure that any competitive issues that are present are managed to provide for a "level playing field" among all providers of telecommunications services. The major issue brought to light by the telecommunications industry is the ability of government to access financial resources that may not be available to private providers. Another important concern was the different treatment afforded public providers in the areas of pricing, regulations, and licensing requirements.

Quality Control and Accountability Issues:

Lack of quality control and accountability to customers was seen as one reason for the legislature to recommend changes to the way that the state engages in telecommunications activities. Ultimately, the difference between private providers and public providers is the need to succeed and prosper by delivery an effective service at a cost-efficient price. Private providers risk being taken over, or worse, eliminated if they do not offer services in an accountable manner. The state on the other hand, can simply return to the legislature for its biennial appropriation with very little oversight as to the need or effectiveness of the state's services.

Private Investment and Profit Motives:

In the telecommunications arena, technology often outpaces the speed in which governments can react. Private providers, having different organizational structures are often in a better position to take advantage of, or even develop, new and innovative solutions. Allowing the government to expand into the state's telecommunications infrastructure may limit the ability to encourage entry into the market and possibly have serious effects on the state's economic future, including the loss of tax revenue from an industry that is one of the fastest growing segments of the economy.

Private providers are required to make a profit for their investors in order to stay in business. Since a public provider does not pay taxes nor required to generate a profit, it does not have to consider these factors when determining what it feels is the cost for the delivery of the service.

One respondent described the current situation in telecommunications to that of the rural electrification policies of the late 1930s. During this period, the government offered a number of advantages to electrical providers to serve areas that represented uneconomic investments. In this case, the respondent suggests that government should be providing services only to those areas where private investment would be cost prohibitive. In essence, the public policy implemented by the state should be to ensure the provision of telecommunications services to those communities where a private provider would have to set rates that most people would be unwilling or unable to pay.

State Video-conferencing:

Much of this group's concern was levied at the state video-conferencing facilities. There does not seem to be agreement among the respondents about whether the state should continue to offer this service at all given that a viable private alternative exists. Some remarked that the state should only offer this service to other governmental units. Others wondered whether the existing facilities should be contracted to the private sector with the state monitoring the contract.

Revisit House Bill No. 515:

Finally, one respondent revisited the principles of the first version of House Bill No. 515, and expands on some key areas. What follows is quoted directly from the questionnaire.

First, there should be an overriding government policy determination that goods and services should be provided by the private sector under all but exceptional circumstances. The Committee/Legislature should consider enacting an outright prohibition against government provision of goods or services in certain industries where private sector provides alternatives to government goods or services. Only where no reasonable private alternative exists should government be allowed to consider provision of a product or service. In such circumstances, there should be a process by which any government provision of goods or services is subjected to public

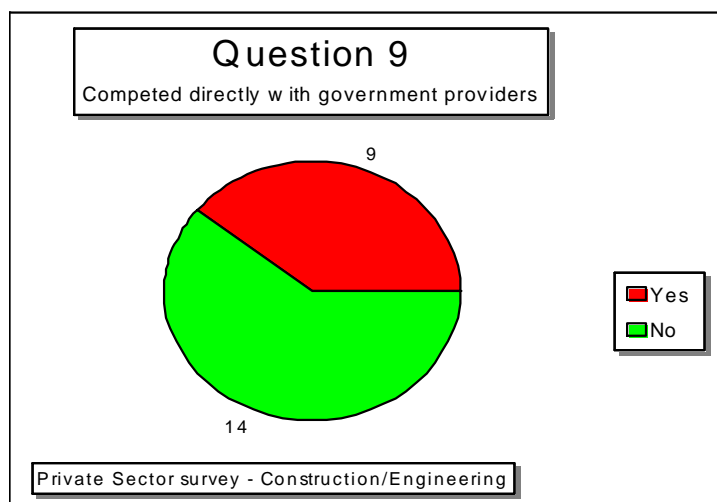
notice, comment and review. After sufficient public notice of government's intent to provide a product or service, there should be provided an opportunity for review of government intentions through an independent "Review Board." The Board should be given clear yardsticks/criteria (i.e., a "checklist") by which to compare the costs and benefits of providing goods or services through government or private enterprises. The Board should be given such authority that its determinations should be both enforceable, yet appealable. That is, the Board's decisions should carry enough weight to effect government actions; if the Board determines a government service should be provided by the private sector, the government entity providing the service should cease and desist. One policy option (though not exclusive of others) may be to require the Board to rule within a given time on any case before it, and to submit its ruling to the Governor who must either act or affirmatively decline action within a given time. The Board's decisions and Governor's action would be publicly available, thereby subjecting the Board's and Governor's actions to additional public scrutiny. On the other hand, both the government and private sector should be able to appeal the Board's decisions, likely to the district courts.

Many of the concerns raised by the telecommunications providers revolve around whether governments in Montana are doing enough analysis to provide decisionmakers with information that is adequate for making informed decisions about where the state should be moving in the telecommunications age. There are examples demonstrating that heavy government involvement in the actual providing of services has resulted in services that are antiquated and too expensive to transfer to the private sector.

Construction and Engineering Fields: Highlights and Recommendations

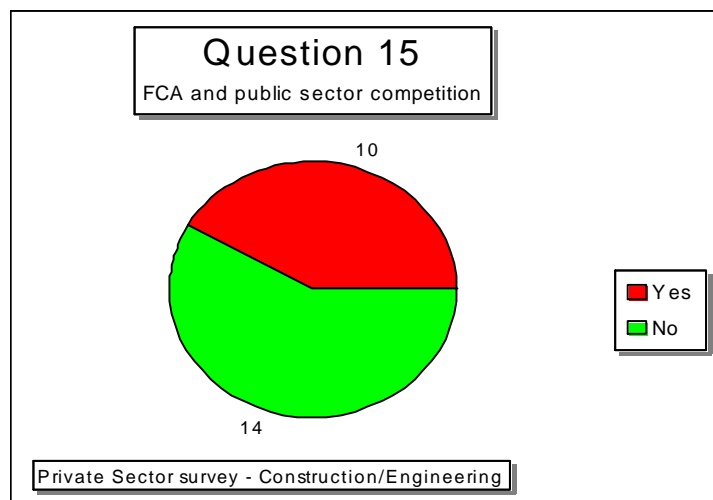
Approximately half of the respondents identifying themselves as members of the construction or engineering field remarked that they provide similar services as public entities do, but they may or may not compete with those public entities. The initial analysis suggests that construction is one field where governments may be more inclined to contract for necessary work. If that proves to be the case following further investigation, it is important to establish contracting policies and procedures that offer governments and private contractors a clear understanding of the project needs and requirements. The charts are on the following page.

Q9. Has your organization competed directly with a governmental entity for the provision of goods or services?



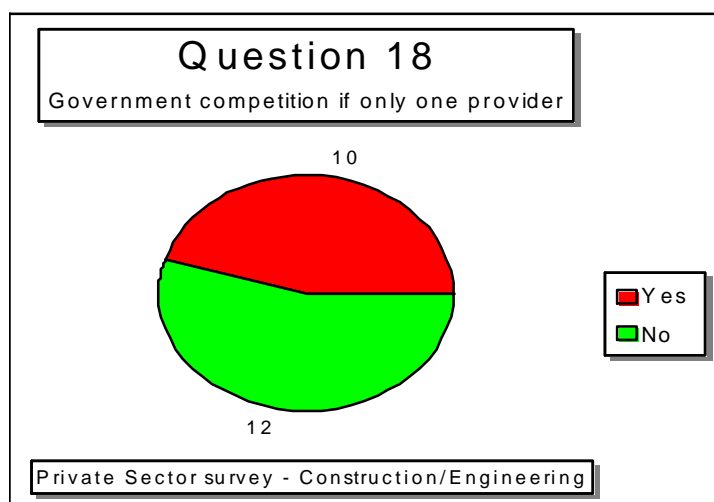
Nine of the fourteen respondents in the combined construction and engineering category stated they did compete directly with government entities. The examples included installing sprinkler systems at golf courses, roofing activities at school districts, road maintenance, repair, and construction, excavation work, and design services.

- Q15. If a methodology was developed to accurately compare the costs of producing and delivering a service by both government and private vendors, would you favor allowing government to compete with your organization?



Question 15 requested information about whether the government should be allowed to compete if a full cost accounting methodology were developed to account for the true cost of providing a service. Again, this industry was fairly evenly split. A few offered additional comments to clarify their answers. Those that responded in the negative stated that governments should not be competing unless there is a clear public benefit accrued from the competition. Several mentioned that an independent body should conduct the costing approach to ensure that it was accurate and reflects methods utilized by private sector businesses.

- Q18. If there is only one private provider of a particular product or service, should government be allowed to compete with that vendor?



The responses to question 18 are evenly apportioned between the two choices. Again, the question indirectly raised the issue of monopoly providers. Careful crafting of contract language, complete with performance measures, oversight, and management would ease the chances that single private providers would take advantage of their position.

Identifying the True Costs of Service:

The general theme of the construction/engineering responses is the development of appropriate costing models that reflect the true cost of providing services. The construction industry responses note that it will be difficult to create conditions under which governmental entities can identify those costs. One respondent cautioned the Committee by saying that there are services that governments can provide more effectively and efficiently. Developing a sound model to determine what those services are should be the Committee's goal.

Taxation:

Another recurrent theme was the issue of taxes. Government entities that engage in construction activities do not pay taxes on equipment, fuel, or tires. A private contractor pays these taxes, as well as others, including the 1 percent contractor gross receipts tax on public projects.

Different Standards:

Several respondents identified a concern regarding the government's exemption from furnishing performance bonds or special insurance policies. In line with this is the apparent disconnect between construction project inspection procedures. Contractors are concerned about the fact that they are subject to regular review by independent parties and the ensuing quality control costs. These requirements are not applied consistently to government construction projects.

Project Monitoring:

A final issue raised relates to the issue of the actual cost of projects, both how that cost is determined, as noted earlier in this section, and how those costs are tracked throughout the life of the project. In essence, the contractor must perform the work for the bid price and insulate taxpayers from cost overruns and contingencies that arise. Government contractors, on the other hand, are not under the same motivation to ensure that projects come in on time, or on budget.

If there are recommendations to be gleaned from the contractor responses, it may be this. First, require that costs associated with government projects be allocated like those of private projects. This will allow decisionmakers to treat both parties consistently which should result in a good service that is a good value to the state's taxpayers.

Health Club Facilities: Problems and Recommendations

Respondents representing the health and fitness industry replied to the questions asked as well as questions not contemplated. Specifically, many members of the health club community suggested that competition from the public sector was not the issue, rather competition from private, non-profit providers was the problem. Clearly, however, government competition is a concern. According to the respondents both situations represent competitive inequities that harm private, for-profit providers of health club services and facilities. Hospital facilities, YMCA's, and Rocky Mountain College were identified specifically. Additionally, one respondent provided information regarding a grant program operated by the State that inadequately represented the community health and fitness needs and existing facilities.

The main public competitors are the University system and local governments that offer recreational opportunities like tennis lessons, weight room facilities, swimming pools, etc. Since there was little information offered by local governments that clearly established a competitive arena, the Committee may wish to investigate this issue in more detail. Clearly, the implication offered by this industry is that the University system facilities managers are offering memberships or services to the public at large, rather than confining the facilities to University students, faculty, and staff. Similarly, in one instance, a city's police department houses a gym that presumably allows the general public access to its facilities.

Recommendations relating to resolving public-private competition include:

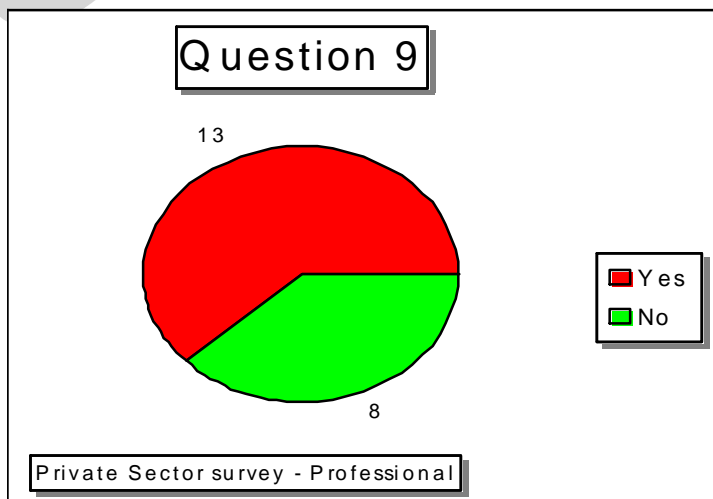
- C Require public entities to pay taxes;
- C Require governments to conduct a true service cost analysis; and
- C Restrict usage of public university facilities to students only.

Professional Services: Recommendations

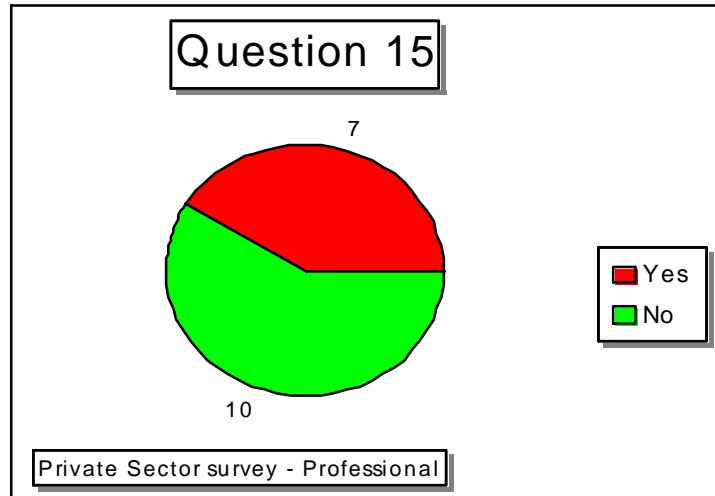
Professional Services represented approximately 21 percent of the total responses. The survey defined professional services as financial, legal, consulting, and human resources operations. Insurance providers, many of whom specifically listed themselves in the "other" category, have been included within this industry group. Again, questions 9, 15, and 18 were chosen for this analysis. The following charts provide the response breakdown.

The responses to these questions suggest that while more industry members identified government competition as a concern, they seem relatively evenly split on whether incorporating a full cost accounting methodology would reduce any competitive advantages.

- Q9. Has your organization competed directly with a governmental entity for the provision of goods or services?

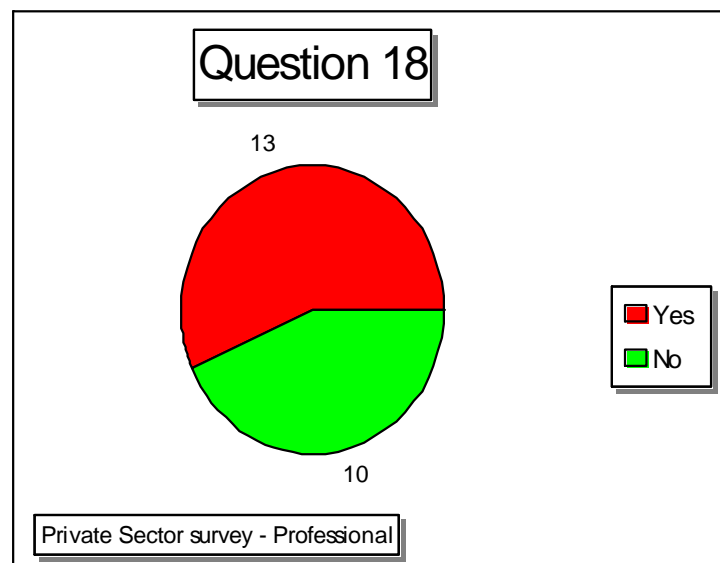


- Q15. If a methodology was developed to accurately compare the costs of producing and delivering a service by both government and private vendors, would you favor allowing government to compete with your organization?



In response to question 15, one respondent remarked that government should conduct an accurate cost allocation for services it provides to other government entities but should not be allowed to compete with private vendors for services delivered directly to the public at large. Others referenced the fact that the Committee should consider reducing the government's involvement by facilitating a partnership with various private entities to realize cost savings when appropriate, but also allow private vendor ability to react quickly to changes in technology, for instance, to benefit the public receiving certain services. Finally, a comment was made regarding the development of functional service boundaries. In essence, the Legislature should identify where government must be involved and develop restrictions to ensure that government service delivery is contained within those boundaries. Presumably, this would allow for greater private sector involvement and perhaps the creation of partnerships, where appropriate, between public and private organizations.

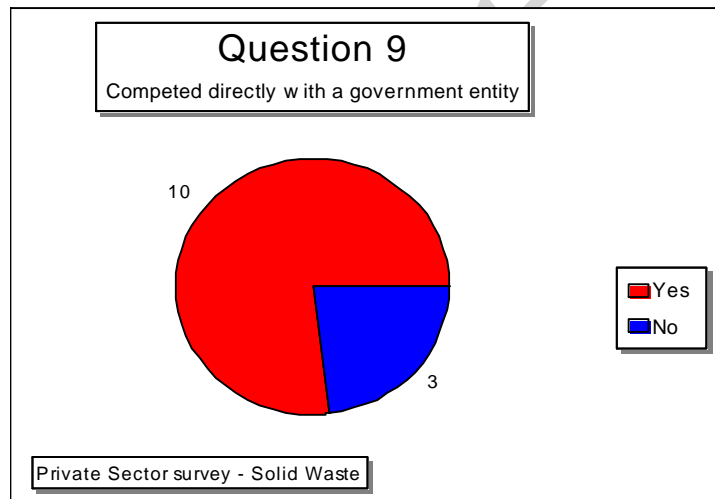
Q18. If there is only one private provider of a particular product or service, should government be allowed to compete with that vendor?



Solid Waste Services Providers: Recommendations

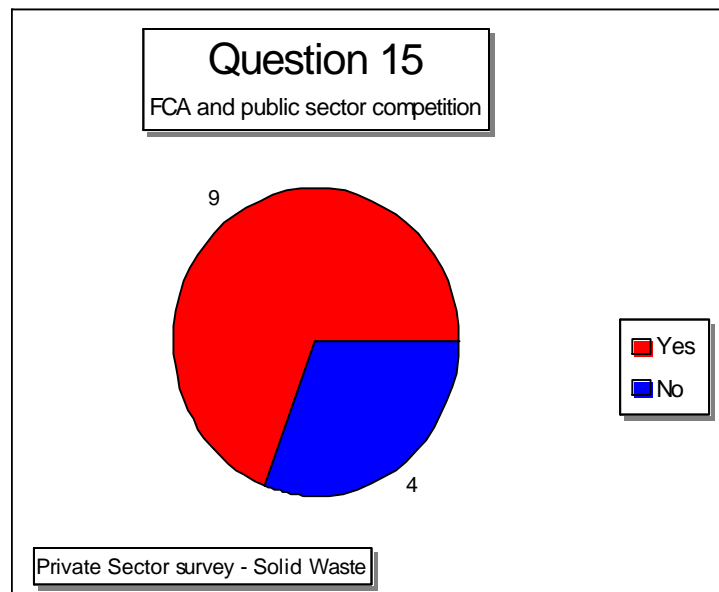
It should be no surprise that every private solid waste services provider stated that they face government generated competitive inequities when it comes to delivering their services to the public. The following three tables represents the solid waste providers responses to questions related to competitive practices they currently face, whether or not public entities should be able to compete after developing and following a full cost accounting methodology, and whether or not public providers should be allowed to compete in instances where there is only one private vendor. The charts are found below.

- Q9. Has your organization competed directly with a governmental entity for the provision of goods or services?



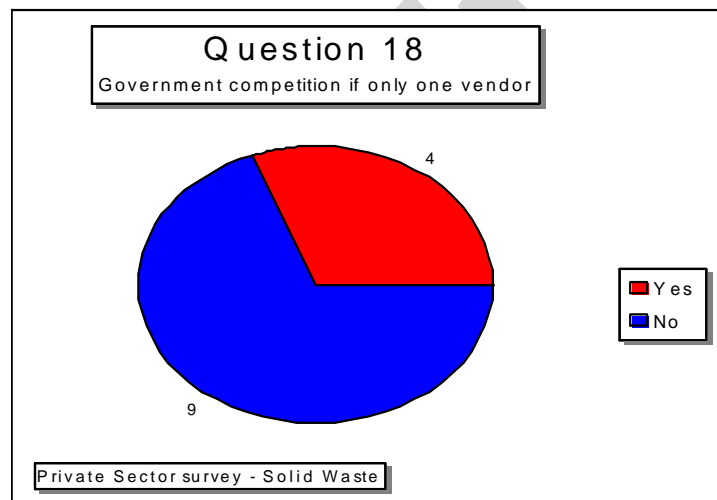
Ten of the fourteen respondents stated that they are in competition with government entities in the area of solid waste services.

- Q15. If a methodology was developed to accurately compare the costs of producing and delivering a service by both government and private vendors, would you favor allowing government to compete with your organization?



Nine respondents stated that they would agree that governments should be allowed to compete if a methodology incorporating the principles of full cost accounting were required of all public solid waste operations. The requirement for full cost accounting was the most mentioned recommendation for reducing the solid waste industry's concern regarding public/private competition. Their rationale, like that of other state's requiring a different model for identifying costs, is that full cost accounting offers governments several benefits, the least of which is the ability to make informed decisions about who should provide certain services. If full cost accounting is required, solid waste customers, regardless of whether they are serviced by a public or private provider, will have a better understanding of what the service truly costs and can make a better determination if the service they receive is a good value.

Q18. If there is only one private provider of a particular product or service, should government be allowed to compete with that vendor?



The final question reviewed is whether or not governments should be allowed to compete if only one vendor is available. The industry responded differently to this line of questioning than they did for the previous one. Four responded that the public sector should be allowed to compete, while nine replied that government should not be allowed to engage in solid waste service delivery. Perhaps a more appropriate question would have considered the implementation of a full cost accounting model in this case as well. A few respondents recognized the design behind the question and countered that if the contract is well drafted to consider issues like performance standards and accountability measures, the public would be well served by the private provider. In essence, due diligence in the contract development would address the overarching question of monopoly providers.

"5-year Rule":

Another recommendation made by several respondents was the need to repeal what is commonly referred to as the "5-year rule." Section 7-13-4107, MCA, enacted in 1979, provides that a municipality receiving solid waste services from a private provider may not elect to begin its own solid waste services unless the municipality first pays the private provider the fair market value of the equipment used by the provider. As the section is written, it also allows the municipality to inform the private provider that it intends to provide its own solid waste services, but will delay the initiation until 5 years have lapsed. If the municipality opts for this approach, it does not seem to be required to pay the private provider for the market value of the collection equipment.

Full Cost Accounting:

Several respondents asked the Committee to recommend to the full legislature a requirement that all solid waste services be subject to Request for Proposals (RFP) so that communities can make better decisions about the costs associated with solid waste services. There are numerous private providers in the state that are capable of serving these communities. This in one sense is what has been referred to by cities employing alternative service delivery programs as the "yellow pages test."

The following represents a summary of the comments made by the private solid waste service providers.

- C Inconsistent application of regulatory requirements between public and private providers.
- C First and foremost, public providers do not pay taxes that private providers must pay. If public providers offer services, they should be required to pay taxes where private provider options are available.
- C The greatest disadvantage comes from the government's ability to arbitrarily assess every property in a district without regard to their actual use of a service.
- C Private solid waste services providers do not have access to a variety of subsidized loans and grants that are available to government providers.
- C Different methods of billing create the impression that private providers are more expensive than government providers.
- C Government providers can often acquire equipment at prices that are significantly lower than what a private provider has access to.

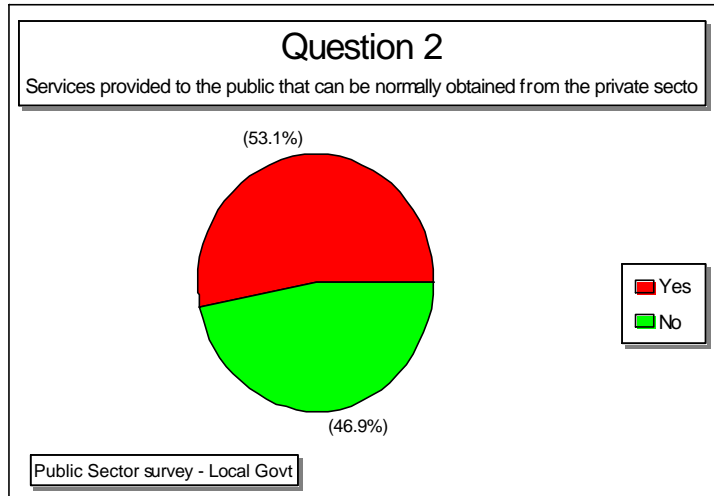
The issues identified and solutions recommended for resolving competitive issues by the solid waste providers in Montana are consistent with providers across the country. There is a significant body of information and knowledge available to the Committee if they choose to concentrate on this issue for the remainder of the interim.

Local Government Analysis

The public agency survey was sent to both county governments and cities and towns. Two major themes were represented by local government entities. First, local government generally responded that they have the ability to make informed decisions regarding how to best serve their constituents. Secondly, the size and demographic makeup of local governments make proposing a broad policy prescription concerning privatization efforts difficult to implement. In effect, such an action could render some small, rural local governments without the available resources to accommodate the Legislature's policy choices.

It was clear that local governments have taken many of the suggestions offered by proponents of privatization or contracting seriously. In essence, when local governments have the ability to make decisions to contract for certain services, they do so. The following charts represent answer to a few key questions.

- Q2. Does your organization provide to the public goods or services that can normally be obtained through the private sector?

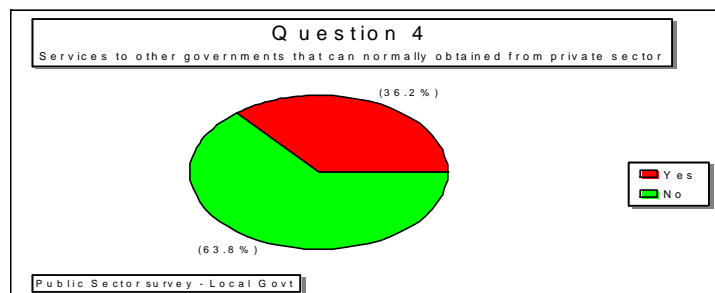


According to local government responses, approximately 53 percent offer services that can be normally obtained in the private sector. The services identified included:

- C Solid waste services;
- C Water sample testing;
- C Park and trail maintenance;
- C Street maintenance;
- C Wastewater systems, water delivery systems, and sewer and storm drain maintenance;
- C Detention facilities;
- C Convention and recreational facilities;
- C Data-processing and other software technical services;
- C Weed control; and
- C Ambulance services.

There are a number of other services identified by local governments that they suggested could be "normally" obtained from the private sector. Like the state respondents, several local governments objected to the phrase "normally obtained" as being judgmental or subjective.

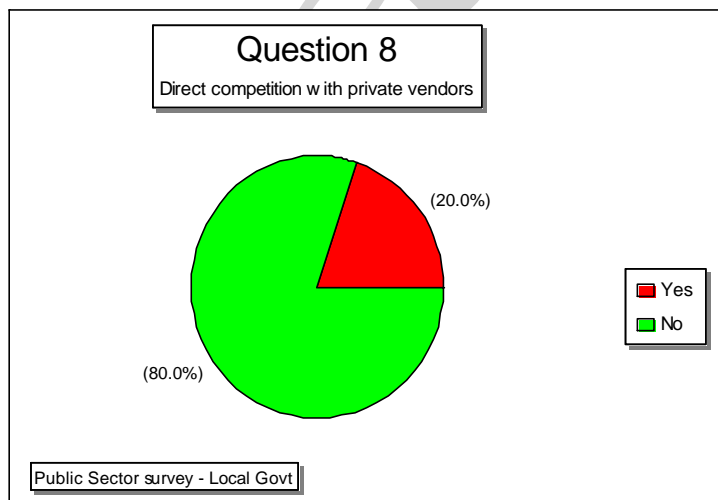
Q4. Does your organization provide to other governmental entities goods or services that can normally be obtained through the private sector?



About 36 percent suggested they did provide services to other governmental entities. The main service identified appeared to be solid waste related services. Ambulance services, wastewater and stormwater facilities, and maintenance operations were also mentioned.

The chart showing the percentage distribution of answers to question 8 is shown below. Eighty percent of the respondents replied that they do not directly compete with private vendors. Of the 20 percent that do compete, the main service was solid waste related services. Again, the difficulty in determining the true nature of public/private competition lies with definitions. As was shown in the chart related to question 2, more than half of the respondents stated they did offer services that could be obtained from other sources. Twenty percent of those same respondents that say they are directly competing would suggest that some competitive bidding process has been established. Confirming this fact from the survey returns is difficult. Some insight was given however, by some respondents, when they suggested that they have competed in the past, but made the determination at a later date to obtain services from a different source.

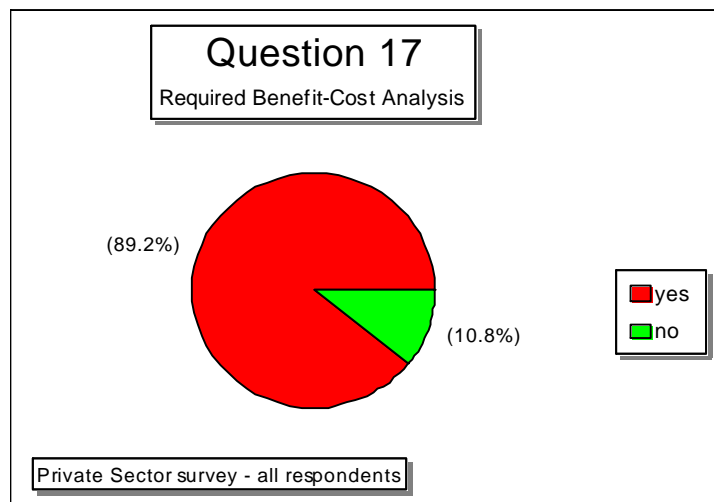
Q8. Has your organization competed directly with a private sector vendor for the provision of goods or services?



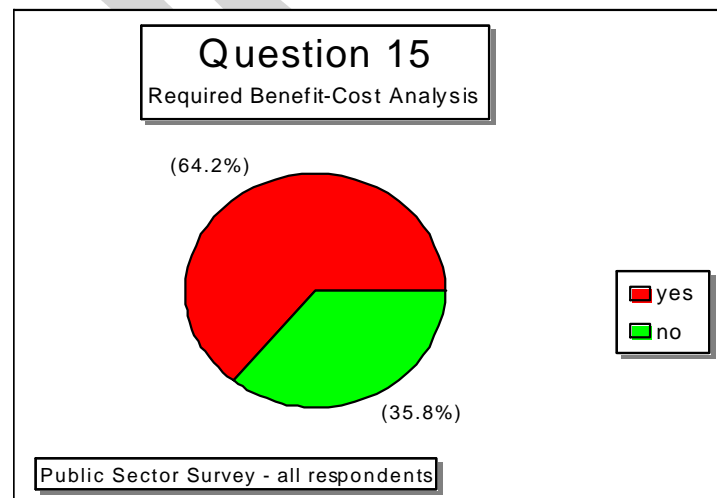
As was raised in the introduction to the local government analysis, several respondents offered information related to the fact that when contracting for services is in the best interest of the public, contracts are established. If the reverse is true, decisionmakers continue to provide services in-house. One of the Committee's tasks was to try and determine how governments come to the decision of establishing what was in the public's best interest.

On the issue of how governments make decisions regarding the delivery of services, each survey asked a specific question related to the requirement of benefit-cost analyses to determine which entity, public or private, is best suited to provide the service. The following two charts show the individual responses. The public entity responses were fairly similar and have been combined to illustrate an overall public entity position.

- Q17. If government has been asked by the public within its jurisdiction to provide a service or product, should government decisionmakers be required to conduct a benefit-cost analysis to determine who provides the services (e.g., public or private vendors)?



- Q15. If government has been asked by the public within its jurisdiction to provide a service or product, should government decisionmakers be required to conduct a benefit-cost analysis to determine who provides the services (e.g., public or private vendors)?



Nearly 90 percent of the private sector respondents stated that governments should conduct a benefit-cost analysis to determine who should provide a service. On the public sector side, close to 65 percent believed the required benefit-cost assessment would be a valuable tool. What the survey could not establish was what variables should be included in the analysis. It would seem that if the Committee were to consider requiring a service delivery analysis that it concentrate on establishing some essential guidelines and expectations to ensure that the process resulted in useful information.

Potential Findings and Items for Committee Discussion

Finding I: The methods used by public entities to account for costs seem to differ from the methodologies used by the private sector.

Question: Should the Committee work with public and private entities to develop a methodology that allows a comparison of costs on a competitively neutral basis?

Question: Should the Committee investigate the benefits and costs of creating and implementing a full cost accounting system for public entities? Should the implementation be conducted on a wide-spread basis or on a narrow, program specific basis?

Question: What are the capabilities of the existing accounting system and what changes, if any, would be needed to accomplish a competitively neutral cost analysis?

Question: For what purposes will the cost allocation information be used? Can a methodology that is developed be used to serve more than one purpose (i.e., budgeting tool, privatization tool, or some combination of both)?

Question: If the information will be used as one component to determine whether some form of privatization is desirable, will comparing the costs of private entities with public entities pose a problem for private vendors (assuming issues of confidential information)?

Question: What organization is best suited to evaluate the information to determine the viability of privatizing certain services?

Finding II: The structure of the public sector entity seems to affect decisions regarding public-private competition.

Question: Should the Committee focus its attention on state government, local government, or some combination of both?

Finding III: Local governments, more so than state government, seem to rely more on constituent requests for services than any established organizational structure outlining whether services should be maintained in-house or contracted to the private sector.

Finding IV: There seems to be dissimilar operating definitions of competition.

Question: Do private vendors feel that access to the opportunity to provide services is a competitive issue?

Question: Should the Committee consider offering their own operating definition?

Question: Should the Committee look to recommending a policy that modifies the way that private vendors do business with the government (through contracted services)?

Finding V: Only one response approached the question using the provisions developed in the original House Bill No. 515.

Question: Should the Committee revisit the original bill or create a new approach?

Finding VI: It is difficult to measure the intensity of concern over government competition. It does seem that even if private vendors do not feel strongly about public-private competition, they do seem to have a strong concern that public entities are not required to comply with regulatory, licensing, or other policies and procedures that govern private entities.

Question: What are the implications of requiring public entities to adhere to the same rules addressing private entities?

CONCLUSION

One of the outcomes this survey was designed to accomplish was to determine whether the competitive issues associated with public/private competition were industry specific or common problems for all private service providers. Another outcome was to determine whether the question the Committee should be asking is why do governments choose to provide certain services and how do they make those decisions?

The responses from the private sector seem to suggest that, regardless of industry, issues associated with public/private competition are similar. It would also seem that many of the suggestions for mitigating the problems identified would generally benefit all private sector providers. This may be especially true in the case of implementing a full cost accounting approach and the requirement that government entities conduct a benefit-cost service delivery analysis before determining which provider would provide a service.

One initial impression of the survey returns might seem to indicate an inconsistency in the definition of the concept of competition. After considering the responses from both groups, the Committee may wish to attempt to determine when the issue is one of opportunity to provide a service and when the issue is one where a government entity is actively competing for a share of the service market that private providers currently have. In essence, does public/private competition exist if there is no process in place to determine the customer base? Clearly, both groups have identified instance where a finite customer base is present and both entities are providing a service that forces the customer to choose who ultimately serves the customers needs. The goal of the Committee is to determine if a public entity is making a decision, conscious or otherwise, to restrict a competitor from gaining access to the customer base. This is a reasonable definition of unfair competition. Another way of approaching this issue is whether a public entity, providing services to itself, is in competition with a private entity capable of delivery a similar service. The survey was not suited to asking customers if they made a choice between a public or private provider.

The question that asked whether government should be allowed to compete if there is only one vendor was designed to illicit a certain response. The reason for this question hinged on the notion that should privatization be proposed for any variety of services, should governments be allowed to enter into the mix in order to achieve the benefits of a competitive market. Several states and local governments across the country have engaged in a system called managed competition. Within a managed competition system, the public entity is allowed to offer a competitive bid to decisionmakers in direct competition with private bidders. Some private vendors are cool to the idea of allowing governments to compete with their business if there are no assurances that the process is competitively neutral. The literature on this subject views managed competition from a balanced perspective. While it may be successful in certain service delivery areas, it does not result in successes in all service areas. Also, the mind set of the private vendors affects whether the managed competition system would be successful. In essence, proponents of managed competition point to the free market as the deciding factor in creating good conditions for service delivery. Encouraging competition, whether among private vendors or public and private vendors should spur innovation, potentially reduce costs, and create program efficiencies and effectiveness. Clearly, public and private vendors would have to trust that the process to implement this system is competitively neutral.

As mentioned, though the survey responses cannot, nor should they, be used to represent a statistically significant sample of private and public opinion, the responses may represent a reasonable assessment of the scope of the issue and a number of potential conclusions. The Committee may be able to narrow their questioning in a manner that would yield possible legislative recommendations. Based on what all of the respondents are saying, in conjunction with meeting testimony, personal conversations, and general Committee discussion, the points made in the findings section of this paper are worthy of additional investigation with an eye toward developing recommendations.

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